

# REGIONS DOUBLING DOWN OR DIVERSIFYING

Exploring economic specialisation vs diversification in Regional Australian mid-sized towns

Each of Australia's smaller cities and towns are facing the challenge of either doubling down on what they are best at, or diversifying.

Our smallest settlements tend to be highly economically specialised and built around a particular industry or business. Our mid-sized towns with between 5,000 and 50,000 residents are much more mixed.

Here are six key points for regional areas to think about when it comes to economic specialisation or diversification.

There are **182 mid-sized towns** in Australia with populations between **5,000 and 50,000**



**1** The performance of urban centres varies over time in line with broader economic conditions, including – in the case of the mining industry – global demand for mineral resources.

**2** The available evidence suggests that **mid-sized towns with a population of 5,000 to 50,000 are more likely to experience strong growth if their economy is more specialised**, and becomes more specialised over time.

**3** **Diversification of the economy may be more important in small towns** (with a population of fewer than 5,000) as it may reduce the risks associated with a smaller population, and for already specialised towns looking to stimulate growth.

**4** **A more specialised economy is likely to generate stronger economic growth and higher per capita incomes** in a population of 5,000 or more, but is also likely to generate fewer jobs than a diversified economic base.

**5** To be successful in the long term, mid-sized towns need to take advantage of the economic opportunities available to them – moving towards specialisation when a particular sector is growing strongly, and diversifying at other times. In this sense, **mid-sized towns need to apply a wide-ranging portfolio of growth strategies.**

**6** The industries or sectors where a regional centre exhibits strength have a large impact on growth rates. Put simply, **places with fast growing industries grow more quickly, and those reliant on slow-growing industries are likely to experience more sluggish growth.**

## KEY TERM DEFINITIONS



A **specialisation strategy** is about growing an economy through promoting specific existing industries based on the depth of a town's competitive advantage or strength.



An industrial **diversification strategy** attempts to expand an economy through growing the breadth of its industry base.



**Related variety** attempts to capture positive externalities between technologically similar industries, such as improved access to labour and supporting services, knowledge spill-overs between firms, and the creation of a local market. An example is drawing on an automotive engineering specialisation to manufacture lawnmowers.



**Unrelated variety** attempts to capture portfolio effects, where diversification across a broad range of sectors can reduce risks arising from volatility in individual sectors. An example is promoting tourism as an alternative to a declining manufacturing specialisation.

# WHAT'S THE BEST PATH?

The answer depends on your community's size and the nature of your specialisations.

**Specialisation can benefit local economies that are dependent on manufacturing, transportation or education.** Deeper competitive strengths are especially effective when the industry is on a growth path.

**Unrelated variety can help insulate local economies that are dependent on sectors especially prone to volatility, such as**

**mining and manufacturing.** Growth in alternative industries will reduce overall volatility, but commercialisable competitive advantages in new industries will take time to develop.

**Related variety can benefit local economies that are dependent on service-based industries, such as tourism and education, that derive their demand from other sectors of the economy.** Broadening the offer from these service industries can in turn enrich customer experiences and further broaden the customer base.

**Table 1: The effect of different growth strategies on a town's economic performance per local industry**

LOCAL INDUSTRIES	SPECIALISATION	UNRELATED VARIETY (DIVERSIFICATION)	RELATED VARIETY	RECOMMENDED GROWTH STRATEGY
<b>Agriculture; Retail Trade; Public Admin and Safety; Healthcare and Social Assistance</b>	Neutral	Neutral	Neutral	No significant benefits from pursuing specialisation or diversification  Primary determinants of growth appear to be other factors
<b>Mining</b>	Neutral	Positive	Neutral	Unrelated variety can insulate local economy against external volatility, have a positive impact on population and employment
<b>Manufacturing</b>	Positive	Positive	Negative	Specialisation can increase wages Unrelated variety can insulate the local economy against external volatility No benefit from related variety
<b>Accommodation and Food Services</b>	Negative	Neutral	Positive	Related variety is beneficial, but do not over-specialise
<b>Transport, Postal and Warehousing</b>	Positive	Negative	Negative	Pursue specialisation
<b>Education and Training</b>	Positive	Negative	Positive	Build concentration around education and education-related activities;  No benefits from unrelated variety

# RELATED & UNRELATED VARIETY IN THE REAL WORLD



## MINING TOWNS

For mining towns, **unrelated variety** has a positive and statistically significant effect on both population and employment. Mining towns that have diversified their local economies beyond mining and mining-related activities are less susceptible to economic cycles specific to the industry, and less likely to witness declining populations during periods of low growth in the industry. All other relationships are statistically insignificant.



## TRANSPORT HUBS

For towns that serve as regional transport hubs, **specialisation** has a strong positive impact on population, employment and incomes, and both related and unrelated variety have a negative effect on all three measures. In fact, the effect of specialisation across all measures is the greatest across all nine industry groupings included in our analysis.



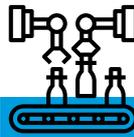
## EDUCATION & TRAINING HUBS

For towns that serve as regional centres for education and training, there are significant benefits from pursuing a strategy of **specialisation** and **related variety**, in terms of their impacts on population, employment and incomes. Concurrently, unrelated variety has a significant negative effect on each of these measures.



## TOURIST TOWNS

For tourist towns with strong accommodation and food service industries, specialisation has a negative effect on population, employment and incomes, and **related variety** has a positive effect on all three measures. The demand for local accommodation services is likely to drive demand for local food and beverage services, and vice versa, by increasing the overall attractiveness of a town for tourists and other visitors. However, if the town is too specialised around tourism and tourism-related activities, that can hinder its growth. The effect of unrelated variety is statistically weak.



## MANUFACTURING TOWNS

For manufacturing towns, the relationships are more complicated. **Unrelated variety** has a positive impact on population and employment, serving as an insulator to external volatility in the sector, similar to the case of mining. Related variety has a negative impact on population and employment, indicating that manufacturing towns should specialise in specific sub-sectors, and there are no benefits to diversifying across different manufacturing activities. Consistent with this point, **specialisation** has a positive impact on income and unrelated variety has a negative impact, suggesting that wage rates in the manufacturing industry are on average better than other industries.

## ECONOMIC DIVERSIFICATION & SPECIALISATION IN BROOME, WA

Broome started as a small hamlet for the export of cattle. As a very small town it had a high level of diversification. Then along came pearling, initially just another diversified arm but soon growing to a significant industry. As the town grew, it became more specialised and this deep specialisation drove and allowed for related and unrelated variety. While proportionately the town was now highly specialised, the quantum of diversified businesses had grown markedly, and these diversified businesses were all pressing to become the next specialisation. As pearling declined the town became more reliant on its diversified base for employment. However, none of the existing industries were sufficiently advanced to act as a point of specialisation. The town stagnated but was assisted in part by government shifting its assets from Derby (which had declined even more). Eventually, one of the diversified industries took off (tourism) and became the next point of specialisation. With the economic activity and jobs from this increasing specialisation, other new related and unrelated businesses were able to be set up, so again increasing the quantum of diversification (some looking to be the next big thing) even while the measures of specialisation show the town as becoming more specialised.



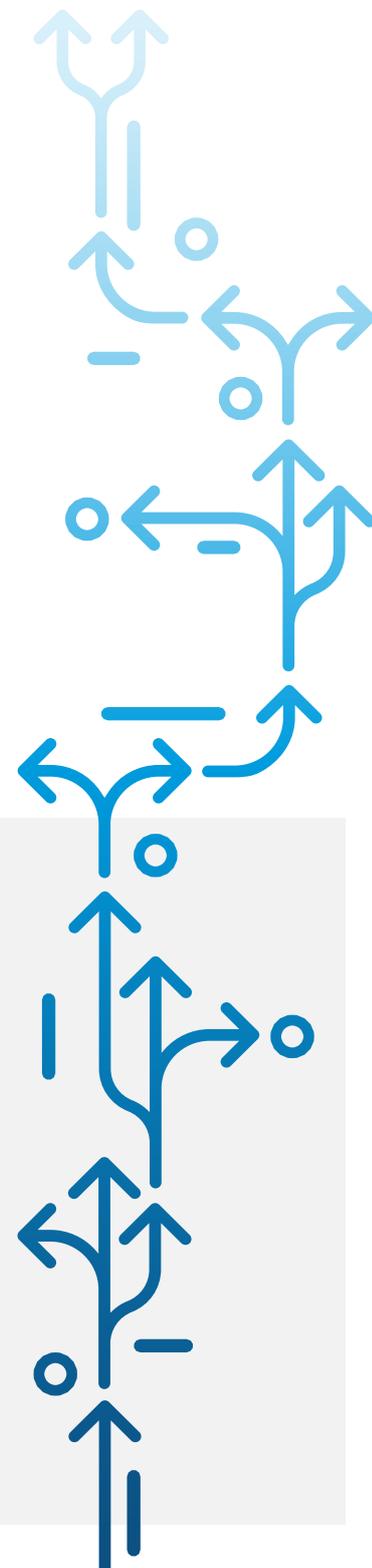
# POPULATION, EMPLOYMENT, WAGE GROWTH – WHAT’S THE GOAL?

Local economies can take different paths, and each path will lead to a different destination. The nature of the new jobs created is the key to whether there’ll be growth in the number of jobs or in the wages achieved, or both.

Specialisation has a positive effect on population and labour force size, but a negative effect on wages. Unrelated variety has a negative effect on wages, and related variety has a positive effect on population and labour force size.

**Table 2: The effect of different growth strategies on a town’s performance per growth goal**

GROWTH GOAL	SPECIALISATION	UNRELATED VARIETY (DIVERSIFICATION)	RELATED VARIETY
<b>Population</b>	Positive	Neutral	Positive
<b>Labour force size</b>	Positive	Neutral	Positive
<b>Wages</b>	Negative	Negative	Neutral



## STRATEGIES SHOULD VARY BASED ON SIZE AND GOAL

Smaller mid-sized towns looking to grow should look for a specialisation to grow through, or in the absence of that, invest in diversifying until a suitable specialisation is found.

Larger mid-sized towns with an existing specialisation should invest in diversity (through a related pathway) to grow incomes, better shock-proof them, and potentially to find a new or the next multi-specialisation.

Large mid-sized towns without specialisation should invest in unrelated diversity until a suitable specialisation is found.

All mid-sized towns should invest in their specialisation until it is well-developed and then look to diversify elsewhere.

**Our research gives strong evidence that place-based growth strategies are required** – each regional town needs its own growth strategy that takes into account how that economy is currently structured. The most appropriate strategy varies from place to place as their economies similarly vary.